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(2000) 10 DEL CK 0036

In the Delhi High Court

Case No : IT Ref. No. 31 of 1980 23 October 2000 A.Y. 1972-73

COMMISSIONER OF INCOME TAX — APPELLANT

Vs

NAGPAL OPTICAL CO. — RESPONDENT

Date of Decision : 23-10-2000

Acts Referred:

Citation : (2001) 164 CTR 338

Hon'ble Judges : Arijit Pasayat, C.J;D.K. Jain, J

Bench : Full Bench

Advocate : Sanjiv Khannawith Ajay Jha and Ms. Prem Lata Bansal, for the Revenue None, for the Assessee, for the Appellant;

Judgement

Arijit Pasayat, C.J.

At the instance of revenue , following question has been referred by the Income Tax Appellate Tribunal, Delhi Bench-D (hereinafter referred to as "Tribunal"), u/s 256(1) of the Income Tax Act, 1961 (hereinafter referred to as ''the Act''), for opinion of this court:

"Whether, on the facts and in the circumstances of the case, the Tribunal is correct in holding that the provision for retrenchment compensation/gratuity of Rs. 35,838 represented an accrued liability for the assessment year 1972-73 and hence was an allowable deduction in computing the business profit of that year?"

2. Brief reference to the factual aspects would suffice:

Dispute relates to assessment year 1972-73 for which previous year ended on 31-3-1972. On 29-3-1972, individual notices for retrenchment of assessor?s employees were served, inter alia, on the following terms :

"As a result of constant dispute among the partners over the economic position of the concern it has now been decided to wind up the business of manufacturing of spectacle frames. This decision of closing down the said business has been taken keeping in view of the economic and industrial trade reasons and to resolve the longstanding dispute among the partners.

The management, Therefore, regret to inform you that your services will no longer be required with effect from 30th April, 1972. This letter which is being served upon you should be considered as one month notice of termination of your service. On the expiry of this notice you will be paid all your outstanding dues including service compensation, etc. You are, Therefore, notified through this notice to surrender your leave cards/ESI cards in the office so that the correctness of your date of appointment be verified and the account be prepared."

Assessee made a provision for Rs. 35,838 towards retrenchment compensation and gratuity and reflected it as liability in its balance sheet as on 31-3-1972. assessed actually paid the amount to its employees on 29-4-1972. The Income Tax Officer rejected the claim of deduction of the amount for the reason that the liability did not accrue during the relevant assessment year. The Appellate Assistant Commissioner before whom an appeal had been filed, endorsed the view of the assessing officer. His reasons for doing so were as follows :

"(i) The notices issued by the assessed did not create by themselves any responsibility to pay retrenchment compensation. The assessed could very well have withdrawn the notices before the due date of payment.

(ii) Services of the employees were not terminated in the relevant previous year. They were terminated only in the subsequent year. The compensation became payable only at the time of termination of the services."

The matter was carried in appeal before the Tribunal by the assessee. Tribunal of the view that though retrenchment was to be effective from 29-4-1972, since notices which were issued on 29-3-1972, had not been withdrawn, assessee, who was following mercantile system of accounting, was fully correct in raising debit in its account for this liability. On being moved, the question as set out above has been referred.

3. We have heard learned counsel for revenue . There is no appearance on behalf of the assessed in spite of service of notice. According to learned counsel for revenue , there being no accrual of liability, Tribunal''s view is not tenable.

4. In this case there was no legal obligation on the part of the assessed to pay retrenchment compensation during the assessment year concerned. Notices of termination were issued on 29-3-1972, indicating to the employees about the intention to retrench them from employment. It was not disputed before the authorities that if the assessed decided to do so it could have withdrawn the notices. Notices issued did not create a responsibility to pay retrenchment compensation. In fact compensation is payable at the time of termination of services. Admittedly services were not terminated during the relevant previous year and were terminated and payments were made in the subsequent year. Therefore, there was no liability to pay retrenchment compensation during the

relevant assessment year. Tribunal''s view is clearly indefensible. What is allowable as a deduction is ascertainable liability in praesenti. Retrenchment compensation u/s 25F of the Industrial Disputes Act, 1947 is allowable as a business expenditure, in case of an assessed following mercantile system of accounting, in the year wherein the liability Therefore is incurred. Till then, it is not a liability in praesenti, but only a contingent liability with the result that a provision therefore, is not allowable. The question, Therefore, has to be answered in the negative, i.e., in favor of revenue and against the assessee.

